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IN THE
Supreme Court of the United States

OCTOBER TERM, A. D., 1940.

No. 291.

EQUITABLE LIFE INSURANCE COMPANY OF IOWA,
Petitioner,

vs.

HALSEY, STUART & CO., A Corporation, *Respondent.*

PETITIONER'S REPLY BRIEF.

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PETITIONER'S REPLY BRIEF.

THE FACTS.

Counsel for respondent preface their brief with a "Supplemental Statement of the Case." While it is said that the statement found in petitioner's brief accords generally with the record, there follows a lengthy recital of the testimony, given principally by witnesses for respondent. In most cases this evidence was directly contradicted by that of petitioner. In presenting this "Supplemental Statement," and indeed throughout respondent's brief, counsel have ignored the rule that in determining the sufficiency of the evidence for submission of this case to the jury, the evidence, and all reasonable and proper inferences which may be drawn therefrom, must necessarily be viewed in the light most favorable to the petitioner.

We shall, as briefly as possible, endeavor to point out the

more important instances in which respondent's "Supplemental Statement of the Case," is merely a statement of respondent's own evidence, and which has been so directly contradicted.

On page 4 of their brief, counsel for respondent urge that the information concerning Longview, which was contained in the circular, plaintiff's Exhibit "B-1," was dictated by the advertising manager for The Long-Bell Lumber Company, and was sent to respondent on April 11, 1927. While respondent's witness Simond so testified, an examination of this circular, and of plaintiff's Exhibits "B-2" and "B-3" (reproduced R. 414-417) discloses that respondent made substantially the same statements with reference to the location of the Long-Bell and Weyerhaeuser mill properties, and the frontage of the city upon the Columbia River, in 1925 and 1926. While Mr. Simond testified that he had never been in Longview, and knew nothing concerning the location or the frontage of the city upon the Columbia River and the location of the industrial plants, other vice presidents of respondent, MacNeille, Shrader and Sleep, were shown to have made at least five or six trips to the City of Longview. (R. 214, 153) Walter I. Sleep, while in Longview in May, 1925, entered into the first contract with the Lumber Company for the purchase of local improvement district bonds. (See Exhibit P-34, reproduced R. 513, 72) Sleep also acted for respondent in acquiring the diking district bonds. (R. 77) Neither MacNeille nor Shrader, although both testified as witnesses in the case, denied knowledge of the location of the Longview corporate limits, and the mill properties. These facts make it clear that in determining whether respondent knew the true facts with reference to the frontage of the city upon the Columbia River, and the location of the mill properties, the jury was not limited by the testimony of respondent's witness Simond. The testimony of Simond that inquiry was made by peti-

tioner for information as to the location of the Long-Bell mill properties; about October 16, is directly contradicted by the testimony of F. W. Hubbell, petitioner's vice president and treasurer. (R. 196, 197) The fact that Hubbell made no such request is further indicated by the confirmation sheets, Exhibits "B-45" and "B-46," by which, on October 16, 1930, respondent confirmed the sale to petitioner of \$200,000 of the local improvement district bonds, and the purchase, from petitioner, on the same day, of a like amount of Chicago Tax Anticipation Warrants. (See Exhibits "B-45" and "B-46," reproduced R. 486, 487) The telegram which Simond claims was sent to Longview for information was not dated until October 16, and reply thereto was not received in Chicago until October 17.

On page 6 of their brief, counsel for respondent state that F. W. Hubbell had been purchasing securities for petitioner for twenty years prior to 1930.

Hubbell testified that he first became active in the affairs of petitioner about twenty years before the trial, which was held in April, 1939. (R. 185) He also said:

"Up until 1928, we were engaged principally in the purchase of first mortgages on farms, and while we had a few municipals for the past twenty-five years, very few to begin with, I would say that along about 1922 we began to enlarge our municipal investment account." (R. 185)

On page 6 of their brief, counsel for respondent state that upon being shown the offering circular, Mr. Hubbell expressed an interest in the bonds, and specifically requested the annual report of The Long-Bell Lumber Company for the year ending December 31, 1929. Hubbell's testimony with reference to this transaction was as follows:

"I asked Mr. Kelley for more information, after looking at this circular, on the City of Longview, what the property was out there, and about the Long-Bell Lumber Company." (R. 187, 188)

Counsel urge, on page 7 of their brief, that the legend appearing beneath the map set forth on the back of Exhibit "B-25," indicates that the map did not purport to show merely the City of Longview, but the entire Longview development, including the industrial area. There was nothing on the map indicating that the industrial area of Longview was separate and apart from the city itself, and if the city had, in fact, a frontage of seven and one-quarter miles upon the Columbia River, as was positively stated in the offering circular, Exhibit "B-1," the whole industrial area was necessarily within the corporate limits.

On pages 8 and 9 of their brief, counsel for respondent state that before purchasing a single Longview improvement bond, Hubbell knew of the existence of Consolidated Diking District No. 1, of the amount of its bonds that were outstanding, of the purpose for which the bonds had been issued, and that such bonds were secured by assessments payable in installments over a period of twelve years. This statement is based upon a paragraph of the Ernst & Ernst letter, which accompanied The Long-Bell Lumber Company's December 31, 1929 balance sheet.

On this phase of the matter Hubbell testified that he read the statement in the letter of Ernst & Ernst which accompanied the financial statement and balance sheet of December 31, 1929, but that the statement did not show where the diking district was located, and that he gave no consideration thereto. (R. 191, 192) The recitals of the Ernst & Ernst letter did not indicate that the City of Longview was embraced within the diking district, and did not disclose that assessments levied for the payment of the diking district bonds were liens upon lands located within the Longview improvement districts. The jury was entitled to consider the facts stated in the Ernst & Ernst letter accompanying the balance sheet in the light of the Wood letter of

May 14, 1930, that "the city has no funded debt other than these improvement bonds."

Again on page 9 of their "Supplemental Statement," counsel for respondent say that in October, 1930,

"Hubbell inquired for the first time whether District No. 11 was co-extensive with the city limits of Longview, and whether the Long-Bell mills were located within the corporate limits of the city." (R. 302)

As we have already pointed out, Hubbell testified positively that he knew that the limits of District No. 11 were practically co-extensive with the City of Longview some time before October, 1930, and denied making any such request.

On page 10 of their brief, counsel for respondent say:

"Contrary to the assertion in petitioner's statement of facts (p. 13) that the Lumber Company defaulted in 1931 in the payment of local improvement assessments on practically all of the improved lots and lands in the various local improvement districts, the facts are that sufficient collections of assessments were made by the several districts so that, at the time of trial, interest coupons falling due in 1936, and, in some cases, in 1937 and 1938 had been paid in full."

This statement is extremely misleading. The assessments in the various local improvement districts were payable in ten equal installments, (R. 247) and were so arranged that had the assessments all been paid, there would have been a fund sufficient to pay interest, and to retire one-tenth of the face amount of the bonds outstanding each year. (R. 247) The bonds, by their terms, were payable on or before twelve years from the date of issue.

Mrs. Faye Scott Witt, City Treasurer of Longview, testified:

"When I came into office, the 1st of January, 1933, the Long-Bell interests had already been unable to pay

some of the installments on property owned by them which they had paid pretty regularly up to and including the year 1930. It was the custom at that time, when it was time to pay interest on the bonds, if the money received from the individual owners did not make the fund sufficient to meet the interest payments, then the Long-Bell Lumber Company made note of that and paid their installments on certain pieces of property in an amount sufficient to take up the interest. The Long-Bell Lumber Company and its subsidiaries did not pay assessments sufficient to enable us to take up the ten per cent of the principal amount of the bonds in the years 1931, 1932, 1933 and subsequent." (R. 248)

Mrs. Cecile Steele, employed as a deputy in the county treasurer's office of Cowlitz County, Washington, at which the general taxes and the diking district assessments were payable, testified:

"The Longview Company, the Longview Suburban Company, the R. A. Long properties and the Long-Bell Lumber Company, paid general taxes upon the real estate assessed in the name of those companies in the City of Longview through the second installment of 1930—that is, they paid their installments that came due in November, 1931, the second half of their 1930 taxes. They did not pay the 1931 taxes due in 1932 on the greater portion of the unimproved tracts. So, a large amount of unpaid general taxes accumulated on their properties in Longview." (R. 266)

In response to a question as to how long that condition continued, the witness said:

"Well, the taxes were unpaid in the fall of 1937. It was necessary for the county to foreclose on them for the 1931 and prior taxes, for which purpose the county instituted a foreclosure action in the Superior Court of Cowlitz County, Washington. The Court gave the County judgment on the property and the County Treasurer was ordered to sell all of the property at foreclosure. He had very few bidders on the sale and the property was deeded to the County." (R. 266, 267)

At pages 10 and 11 of their brief, counsel state that respondent had purchased the bonds, which it sold to petitioner, at prices only a point or two below those at which the bonds were purchased by petitioner, except with respect to one lot of bonds, where, due to special circumstances, respondent was able to purchase the bonds at 89. Counsel omit to inform the court that this one lot comprised \$200,000 par value of improvement district No. 11 bonds which respondent bought from B. M. Baruch of New York City, in October, 1930, at a price of 89, of which respondent resold \$170,000 to petitioner at a price of 99¾. (R. 285) Thus, respondent made a profit of more than \$17,000 on \$170,000 of the bonds purchased by petitioner.

On page 11 of their brief, counsel for respondent indicate that Windsor, petitioner's representative, spent a considerable amount of time at Longview in June, 1931. Windsor testified that he was in Longview but one day. (R. 388)

At page 12, counsel for respondent urge that the statement in petitioner's brief that it made complaint to Kelley that the bonds had been misrepresented in the summer or fall of 1931, does not accurately state the testimony of Mr. Hubbell. Upon this issue Hubbell testified:

"After the receipt of Mr. Windsor's report, in June, 1931, and after the information from Halsey, Stuart & Co. in July and August, 1931, I complained to Mr. Kelley about the bonds. (R. 209)

In my complaints to Mr. Kelley, I told him that I thought the bonds had been misrepresented; I said that a number of times. I never wrote a letter making any formal demand." (R. 209)

Mr. Windsor also testified that he discussed the Longview bonds with Kelley on a number of occasions after his return from Longview about July 1, 1931, and made complaint to him that Halsey, Stuart & Co. had misrepresented the bonds

(R. 388-389), and should take them off petitioner's hands. Kelley testified to the fact of complaints. (R. 309-310)

On page 12 of their brief counsel for respondent state that Hubbell continued to buy bonds from respondent, after he was fully advised of all the facts now alleged to have been misrepresented. Petitioner purchased no local improvement bonds after February, 1931. (R. 206, 207) The bonds which petitioner purchased from respondent in 1931, 1932 and 1933 were issues having no connection with Longview, Washington, or The Long-Bell Lumber Company.

At page 13 of their brief, counsel for respondent state that the year 1929 had been a fairly prosperous year for The Long-Bell Lumber Company, and that it looked forward to an improvement in 1930, despite the market break of 1929.

Mr. Jesse Andrews, General Counsel for the Long-Bell interests, testified that the balance sheet as of December 31, 1929, showed an addition to surplus of \$1,591,000, realized in part from profit on the sale of two tracts of standing timber to the Lamm and Kesterson Lumber Companies.

On page 13 of their brief, counsel for respondent urge that the suggestion of the officers of the Chase National Bank that the Long-Bell Company form a new subsidiary, which would own all liquid assets, and conduct borrowing operations with commercial banks, was not given serious consideration by the Long-Bell officers until the latter part of July, 1930. This statement is directly contrary to the evidence of the Long-Bell officers. Thus, in writing Mr. Andrews (Long-Bell counsel), on May 15, 1930, concerning the demands of the Chase Bank, R. T. Demsey, Long-Bell vice president, said:

"Mr. Long assigned to you and to me the job of considering the creation of a new company, as above mentioned, and bringing it into existence just as quickly as

possible." (See plaintiff's Exhibit "W-13," reproduced R. 534)

H. L. Stuart, President of respondent, was consulted concerning the demands of the commercial banks some time before June 30, 1930, for on that date, in writing R. A. Long, Chairman of the Lumber Company, Stuart said:

"I am sure that Mr. Andrews gave you my message, which was to ask you to kindly let me know the outcome of your next talk with the Chase Bank." (See Exhibit "B-12," reproduced R. 442; R. 105)

R. T. Demsey, a Vice President of Long-Bell, testified:

"My general recollection is that Mr. Stuart was present when the New York trip was discussed. I haven't been able to do better in recollecting it than I did yesterday. I can only say that it was the spring or summer of 1930, and I can't place it by months. My recollection is that Mr. Long, Mr. Andrews and myself were present, and I believe it took place in Chicago.

The substance of the conversations was that the Chase Bank in New York had suggested that they thought it would be wise on our part to strengthen the current financial position of the Long-Bell Lumber Company and that one way that that might be done was to create a separate subsidiary, wholly owned by the Long-Bell Lumber Company, to own the liquid resources and do the bank borrowing. My recollection about the situation is that we were explaining this to Mr. Stuart so that he would understand the situation as we found it, and I don't know that there was so much soliciting his opinion as there was counseling with him; but my recollection is, stating it briefly, that Mr. Stuart's comment was that if we found that our ability to carry commercial bank loans could only be worked out by having a separate subsidiary, that that was probably the thing to do." (R. 148, 149)

On pages 14 and 15 of their Brief, counsel urge that the officers of respondent did not regard the formation of the Long-Bell Lumber Sales Corporation as reflecting in any

way upon the financial integrity, or solvency, of The Long-Bell Lumber Company. While both Shrader and Stuart testified in accordance with this statement, it would be strange, indeed, if the jury gave full credit to such an impossible story. For several months prior to May 1, 1930, the Long-Bell executives had been pleading with respondent to do additional financing, pointing out the need for Long-Bell to "strengthen its current cash position," and that additional financing was particularly necessary because of the "nervous, critical and sensitive attitude" of Long-Bell's commercial bank creditors. (R. 436) For several months prior to May 1, 1930, the Long-Bell executives had been begging for additional loans, even going so far as to offer a mortgage upon the assets of the Longview Daily News, a Long-Bell controlled newspaper at Longview, as security for a loan of \$150,000.

Respondent's officers, Stuart and Shrader, during this period, were constantly advising the Long-Bell officers, that, in view of the price at which Long-Bell credit was selling in the open market, it was hopeless to undertake additional financing. The jury well knew that Shrader, Stuart and respondent's other officers, were men of large experience in business affairs. Stuart and Shrader both testified that the formation of the Sales Corporation, and the transfer to it of substantially all of the liquid and unencumbered assets of Long-Bell, would leave the Lumber Company substantially no assets with which to perform its guarantee of the diking district and local improvement bonds.

Respondent had marketed more than \$25,000,000 of first mortgage bonds of The Long-Bell Lumber Company, secured by liens upon standing timber and mill properties, including those located just outside the limits of Longview, Washington. It had likewise marketed approximately \$6,260,000 of diking and Longview local improvement bonds, which were unconditionally guaranteed by Long-Bell, as well as an

issue of \$3,250,000 of Long-Bell collateral gold notes, secured by the pledge of all the outstanding bonds of Long-Bell's railroad subsidiary. The formation of the Sales Corporation and the transfer to it of substantially all the unencumbered properties of Long-Bell, plus most of its cash and liquid assets, rendered Long-Bell's guarantee of payment of the local improvement district bonds well nigh worthless.

Hubbell made no personal inspection of Longview until some time in the summer of 1934, when he spent several days there in company with Messrs. MacNeille, Andrews, and others. Shortly after Hubbell's return from Longview, the claim involved in this case was presented to respondent by petitioner, through its attorneys, and is identified as Exhibits "52," "52-A" to "52-L," inc. This exhibit is not reproduced in the record, but will be found among the exhibits certified to this court, and an examination thereof will disclose that petitioner carefully reserved in this written claim, any and all rights to which it might be entitled.

At page 18 of their brief, counsel for respondent urge that after the institution of this suit, petitioner, in its report to its policyholders, was shown to have been carrying the Longview improvement bonds at a valuation greater than set forth in its verified petition. F. W. Hubbell testified that petitioner undertook to comply with instructions of the various insurance departments of the states in which it operated, in the book valuations at which its various assets were carried, (R. 207), and that under the insurance department regulations, when current coupons upon bonds have been paid, they are customarily carried on the books on an amortized basis. (R. 210) At the 1935 year end, petitioner held \$272,000 par value of Longview improvement bonds, which were carried on its books at \$231,200. (R. 202) At the 1936 year end, petitioner had \$266,000, par value, of

said bonds, which were carried on the books at \$26,600, and the book value of the same bonds had been reduced on December 31, 1938, to \$18,620. (R. 208)

SUMMARY OF REPLY ARGUMENT.

I.

The opinion of the Seventh Circuit Court of Appeals gave controlling effect to the "hedge clause" of the offering circular; and in so doing, acted without foundation in legal precedent or authority.

II.

Petitioner has met the burden of establishing by a fair preponderance of the evidence the allegations of fraud.

III.

The furnishing of the January 1, 1930 Long-Bell Lumber Company financial statement and balance sheet, with no explanation that conditions therein shown had materially changed, within respondent's knowledge, the writing of the Wood letter of May 14, 1930, that petitioner had been furnished "substantially all the data," and the writing of the Wood letter of June 4, 1930, stressing the importance of Longview as a commercial center, and the financial strength of the Lumber Company, as indicated by the recent substantial retirement of its first mortgage bonds, are sufficient to carry to the jury the issue of respondent's fraud in indulging in half-truths with respect to the financial standing of the Lumber Company.

IV.

The rule of caveat emptor does not apply in Iowa in all cases in which the parties are dealing at arm's length. The situation of the parties, the subject matter in hand, the

knowledge, and means of knowledge of each of the parties, are to be taken into account upon the question of fraud. This case, therefore, is not one in which caveat emptor may be applied.

V.

The trial court properly ruled that the statements of the Wood letter of May 14, 1930, that

"We believe you have before you practically all the data," and

"You will observe that the city has no funded debt other than these improvement bonds,"

constituted representations that petitioner had been furnished all the facts within respondent's knowledge, that there were no other similar securities outstanding, and that such representations were material. Whether such representations were false, and were relied upon by petitioner, were properly submitted to the jury by the trial court, and the determination of the Seventh Circuit Court of Appeals, that the letter was of "trivial materiality," substituted the judgment of that court for that of the jury on the weight of the evidence.

VI.

A mere reading of the opinion of the Seventh Circuit Court of Appeals demonstrates that it was predicated in large measure upon the thought that had petitioner adequately investigated the Longview, Washington improvement bonds, it would have discovered the true facts, and that its failure so to do bars recovery. This is directly contrary to the rule of law which prevails in Iowa.

VII.

The Seventh Circuit Court of Appeals determined but one question, namely, that the evidence was insufficient to

justify submission of the case to the jury, and that the trial court should have directed a verdict for defendant. No other assignments of error were considered or decided.

A.

The instructions of the court upon the question of damages state correct rules of law for the guidance of the jury.

Stokes v. Converse, 153 Iowa 274, 133 N. W. 709, 711.

Whiting v. Price, et al., 51 N. E. 1084 (Mass.).

Hindman v. First National Bank, 112 Fed. 931.

Baumchen v. Donahoe, 215 Iowa 512, 242 N. W. 533.

B.

Evidence of events subsequent to 1930, in connection with the Longview local improvement bonds, was competent, and was properly admitted in evidence by the trial court, and the effect to be given such evidence was properly covered in the court's instructions to the jury.

Hotaling v. A. B. Leach & Co., 247 N. Y. 84, 159 N. E. 870.

C.

There was evidence before the jury justifying the verdict of Sixty-six Thousand One Hundred Fifty Dollars (\$66,150).

Hotaling v. A. B. Leach & Co., 247 N. Y. 84, 159 N. E. 870.

Crandall v. A. B. Leach & Co., 223 N. Y. Supp. 127.

Paul v. Cameron, 256 N. W. 11 (Nebr.).

Hindman v. First National Bank, 112 Fed. 931.

Baumchen v. Donahoe, 215 Iowa 512, 242 N. W. 533.

ARGUMENT.

I.

The opinion of the Seventh Circuit Court of Appeals gave controlling effect to the "hedge clause" of the offering circular, and in such respect is without foundation in legal precedent or authority.

A reading of the opinion of the Seventh Circuit Court of Appeals demonstrates that that court gave controlling weight to the so-called "hedge clause" found in the offering circular, plaintiff's Exhibit "B-1." Thus, in the opinion of Circuit Judge Sparks, speaking for the court below, it is said:

"As to the first two (representations as to the location of the industrial plants, and the frontage of the city upon the Columbia River) which we think constitute the only actual *misstatements* in the record, appellant (respondent) expressly guarded itself against liability for possible inaccuracy by the hedge clause in the prospectus, as set forth above * * *

Therefore, the hedge clause constituted a valid defense to the charge of misrepresentation as to the location of the plants and the river frontage, and the jury should have been so instructed."

Counsel for respondent, in the court below, urged that the hedge clause constituted a defense to all the charges of fraud pleaded by petitioner, but, in this court, they urge that the court below did not find that the hedge clause relieved respondent from liability for misrepresentations, falsely or recklessly made. Counsel have apparently shifted their position, and notwithstanding the decision of the Circuit Court of Appeals, which adopted their argument, now urge that the Circuit Court of Appeals did not give controlling weight to the hedge clause. A reading of the decision of the Circuit Court of Appeals demonstrates that that

court did regard the hedge clause as of controlling importance.

Counsel now say that the proper function and scope of the hedge clause was merely to advise petitioner that the statements contained in the circular were not being made by respondent of its own knowledge, but were based upon information furnished by others, and believed by respondent to be accurate.

The record demonstrates that the information embodied in the offering circular was neither furnished to respondent by others, nor was it believed by any officer of respondent to be an accurate and correct statement of the facts. The record shows that three vice presidents of respondent made five or six trips to Longview to investigate the various Long-Bell issues of bonds which respondent distributed between 1923 and 1930. None of these vice presidents denied knowledge of the location of the Longview corporate limits, or the industrial properties. The record shows that instead of entrusting the preparation of the bond circulars to officers who had knowledge of the situation, Mr. Simond, who had never been to Longview, was commissioned to prepare them. Mr. Simond does not claim that he was informed, or even supposed, that the Long-Bell, Weyerhaeuser, Longview Fibre and other industrial plants were within the City of Longview. No officer or employe of The Long-Bell Lumber Company ever gave him such information. He merely prepared the bond circulars, and forwarded them to Mr. Andrews, who now says that he found nothing wrong with them. This was the same Mr. Andrews who testified as a witness that no question existed in his mind as to the financial position of The Long-Bell Lumber Company in the summer of 1930, notwithstanding the demands of commercial banks that the Lumber Company form a new subsidiary corporation, and transfer thereto all of its liquid and unencumbered properties. (R. 351) Mr. Simond now says that when he was con-

fronted with a direct inquiry in October, 1930, as to whether the Long-Bell and Weyerhaeuser mills were within the City of Longview, he felt it necessary to wire the Long-Bell offices at Longview for the true facts. In 1927, in wiring the Minneapolis sales manager of respondent, Simond said concerning the local improvement bond issues:

"We haven't the data, but with exception one or two districts, showing would probably be disappointing from point of population, area, valuations, etc., and for this reason we rely entirely on Long-Bell guarantee." (R. 80, 81)

On November 19, 1926, in response to an inquiry from the Philadelphia office of respondent, Simond wired:

"District No. 11 is a sewer district, formed to complete sewer construction begun by city, and takes in most of the city."

The jury was amply justified, under the record, in finding that respondent and its officers did not actually believe the statements contained in the offering circular and the other exhibits. Under such circumstances, as we pointed out in our original brief, the question of respondent's liability for false and fraudulent statements was a question for determination by the jury, and not by the court.

II.

Petitioner has met the burden of establishing by a fair preponderance of the evidence the allegations of fraud.

At pages 41 to 45, inc., of their brief, counsel urge that fraud is never to be presumed, that it must be affirmatively established by clear and satisfactory evidence, and that in the application of these rules, the Circuit Court of Appeals properly determined that no actionable fraud on the part of respondent was shown. We concede, of course, that fraud

will not be presumed, that the burden of establishing fraud is upon him who asserts it, but we submit that petitioner has fully met this burden.

First, it is to be observed that every charge of fraud made against respondent by petitioner is supported by documentary evidence. It is established beyond controversy that respondent delivered the offering circular, and the other exhibits, to Hubbell for the purpose of inducing the purchase of the bonds. The writing of the Wood letters of May 14 and June 4, 1930, is admitted. The facts with reference to respondent's knowledge of the true financial condition of The Long-Bell Lumber Company were established largely by the admissions of respondent's executive officers, and by correspondence, which such officers admit was conducted over their own signatures. There is no dispute in this record as to the making of the representations. There is no substantial dispute concerning respondent's knowledge of the true financial condition of The Long-Bell Lumber Company. There is no dispute with reference to the positive misrepresentations concerning the location of the industrial plants and the frontage of the city upon the Columbia River. A fact question is presented as to respondent's knowledge of the location of the industrial properties, and the frontage of the city upon the Columbia. The jury in the trial court concluded that petitioner had met the burden imposed upon it by the court's instructions.

At page 45 of their brief, counsel urge that

"All talk about respondent intentionally misstating the facts in its circular regarding Longview, is patently absurd."

Counsel for respondent say that it had not the slightest interest in misrepresenting any facts regarding the City of Longview. Respondent was an investment house,—the record shows, one of the nation's largest, —It had many offices,

and it was engaged, among other things, in maintaining a market for the securities which it had sponsored and originally sold. The argument set forth on page 45 of Respondent's Brief was perhaps proper for consideration by a jury. It certainly has no place, in view of the admitted facts, in a brief before any appellate tribunal. We submit that the evidence of petitioner fully met every burden imposed upon it by law, and that the opinion of the Circuit Court of Appeals merely substitutes the judgment of that court for that of the jury below upon conflicting evidence.

III.

The furnishing of the January 1, 1930 Long-Bell Lumber Company financial statement and balance sheet, with no explanation that conditions therein shown had materially changed, within respondent's knowledge, the writing of the Wood letter of May 14, 1930, that petitioner had been furnished "substantially all the data," and the writing of the Wood letter of June 4, 1930, stressing the importance of Longview as a commercial center, and the financial strength of the Lumber Company, as indicated by the recent substantial retirement of its first mortgage bonds, are sufficient to carry to the jury the issue of respondent's fraud in indulging in half-truths with respect to the financial standing of the Lumber Company.

Under Division III of their brief, pages 46 to 61, inc., counsel for respondent urge that the record contains no proof that it indulged in any half-truths with respect to the financial condition of The Long-Bell Lumber Company. The Circuit Court of Appeals treated the case as presenting nothing more than silence on the part of respondent, not amounting to fraud.

Before proceeding to a consideration of the authorities cited in Respondent's brief, we desire to dispose of the con-

tention that there was no evidence from which the jury could properly find that respondent did indulge in half-truths with respect to the financial condition of the Lumber Company. We have pointed out, in our Brief, that after being shown the offering circular, Exhibit "B-1," Hubbell requested more information concerning the City of Longview, the property, and The Long-Bell Lumber Company. (R. 187, 188) In compliance with this request, respondent submitted to Hubbell the large mass of information, including the January 1, 1930 Long-Bell balance sheet. In submitting the balance sheet, respondent did not advise Hubbell that the conditions therein shown had materially changed by reason of the substantial operating losses suffered by the Lumber Company, and particularly, by reason of the demand of the commercial banks that the Lumber Company create a new subsidiary corporation. After Hubbell had sufficient time to examine the mass of data submitted, Wood wrote the letter of May 14, 1930, Exhibit "B-24." In this letter Wood positively stated that he believed that Hubbell had "practically all the data covering the issue." This, as we have already pointed out, was a clear representation that petitioner had been furnished all the information in respondent's possession on the matter. Respondent, however, withheld all information possessed by its executive officers as to the true financial condition of the Lumber Company.

After the purchase of the \$100,000 of these bonds, Wood, on June 4, 1930, again wrote Hubbell. (Plaintiff's Exhibit "B-40," R. 483) In this letter Wood discussed what he described as a rumor, but which the Long-Bell officers knew to be a fact, that trunk line railroads operating in the Pacific Northwest were about to acquire Long-Bell's railroad subsidiary. With respect to the transaction, Wood said:

"This rather emphasizes not only the importance of this particular asset of The Long-Bell Lumber Company, but also the importance of Longview, Washington, it-

self. * * * Regardless of whether this does, or does not, take place, the reflection of Longview, Washington cannot be other than favorable.

Incidentally, I think you might be interested in knowing that within the past few days they have undertaken the retirement of a very substantial amount of Long-Bell Lumber Company Mortgage Bonds from funds which became available from the sale of capital assets not necessary to the successful operation of this Company."

The fact that a corporation is retiring its bonded indebtedness in substantial amounts, is one of the strongest indications of financial strength and solvency, and Hubbell so understood the Wood letter of June 4, 1930.

Was not Wood, in writing the letter of May 14, 1930, indulging in a half-truth when he stated that Hubbell already had "substantially all the data"? And, again, in writing the letter of June 4, soliciting the purchase of additional bonds by petitioner, did not Wood make the statements concerning the retirement of bonds for the purpose of leading Hubbell to believe that this was an indication of financial strength of the Lumber Company?

In our original brief we pointed out that 23 American Jurisprudence, Fraud and Deceit, Par. 94, states the rule, that

"Very little in addition to non-disclosure of material facts is required to prevent the application of the general rule which renders mere silence non-actionable, and to make a party guilty of fraud."

Here respondent was not content with mere silence. As we have pointed out, it did indulge in half-truths with respect to the financial condition of the Lumber Company, which led petitioner's officers to believe that the facts were vastly different from those which respondent knew to be true. In view of the record, a jury question is presented on this phase of the case.

The first case relied upon by respondent in support of its contention that it was under no obligation to disclose the true financial condition of The Long-Bell Lumber Company, is that of *Gamet v. Haas*, 165 Iowa 565, 146 N. W. 465. There plaintiff brought an action for the recovery of damages, based on fraud in the sale of stock of a corporation known as the Woodbine Milling Company. The property of the corporation consisted of a two story flouring mill at Woodbine, Iowa, where both plaintiff and defendant resided. Plaintiff's son-in-law was the miller in charge of the operation of the corporation's plant. The only charges of fraud made by plaintiff were that defendant did not disclose that the corporation owed a \$3,400 debt covering a part of the purchase price of its property. No inquiry was made by plaintiff for information concerning the financial condition or assets of the corporation, and no such information was furnished by the defendant. The Iowa Supreme Court held that the trial court had properly directed a verdict for defendant, and in the course of the opinion, the court said:

"The parties appear to have assumed mutual knowledge or information, as well they might, for plaintiff's son-in-law was in charge of the property as miller, and plaintiff was familiar with the enterprise. The record is without evidence from which the inference of bad faith might be drawn. As there was no proof of fraudulent representations, it is unnecessary to inquire into the charge of having fraudulently concealed these."

In *Boileau v. Records & Breen*, 165 Iowa 134, 144 N. W. 336, it appeared that defendants held a tax deed covering forty-eight acres of land, which one Kesterson, a former titleholder, occupied. Both parties were aware that Kesterson was in actual, physical possession of the property. Possession of real estate by a third party, under the Iowa law, is constructive notice to the world of his actual rights. De-

fendants traded the tax deed to plaintiff for other properties. Plaintiff paid about one-quarter of the actual market value of the real estate, if the title were good. Plaintiff was a real estate dealer, and was thoroughly conversant with land values in the community. He knew that a suit had been brought against Kesterson to recover possession of the real estate, but did not know whether it had been disposed of by the court where it was pending. After acquiring the tax deed, plaintiff attempted to dispossess Kesterson, but he was held of unsound mind, and the tax deed was held void. The Iowa Supreme Court held that plaintiff had both actual and constructive notice of Kesterson's rights in the property; that he gave a wholly inadequate consideration for the real estate, and that the representation that the tax deed was "regular and in accordance with the laws and requirements of Iowa," was not a fraudulent representation as to the state of the title. There is nothing in that authority which is of the slightest value in determining the question now presented to this court.

The Iowa case of *Sherman v. Harbin*, 125 Iowa 174, 100 N. W. 629, involved fraudulent concealment of the practices engaged in by an officer of a corporation, and is clearly not in point here.

We have already pointed out the half-truths in which respondent indulged. At page 50 of their brief, counsel urge that respondent furnished to petitioner exactly what it asked for, namely the January 1, 1930 financial statement and balance sheet of The Long-Bell Lumber Company. We have already pointed out that Hubbell's request was not specific, but was for additional information concerning The Long-Bell Lumber Company, and the property at Longview. It was in response to this request that the financial statement and report were submitted, with no intimation that the situation therein disclosed had so materially changed that the Lumber Company could only keep afloat by creating a new

subsidiary corporation, and transferring to it all of its liquid assets and unencumbered properties.

Petitioner's charge of fraud with respect to the financial condition of The Long-Bell Lumber Company rests not upon mere failure to disclose, as the Circuit Court of Appeals said, but upon the furnishing of information essentially false and misleading in character, coupled with the statement that such information constituted "substantially all the data covering the issue." The evidence presented an issue for determination by the jury.

IV.

The rule of caveat emptor does not apply in Iowa in all cases in which the parties are dealing at arm's length. The situation of the parties, the subject matter in hand, the knowledge, and means of knowledge of each, are to be taken into account upon the question of fraud. This case, therefore, is not one in which caveat emptor may be applied.

At pages 62-65 of their brief, counsel urge that in Iowa the rule of *caveat emptor* is applied to all transactions where no fiduciary relationship is present, and there is no evidence of fraudulent concealment. This is not a correct statement of the Iowa rule. The only cases cited in support of the statement are those of *Gamet v. Haas*, 165 Iowa 565, 146 N. W. 465, which has already been considered in the preceding division of this argument, and *Wagner v. Standard Seed Tester Co.*, 194 Iowa 1330, 191 N. W. 314. That was an equity action, by a stockholder, seeking cancellation of his certificates of stock, and repayment of the amount paid to the corporation therefor. Plaintiff alleged that he purchased ten shares of the preferred stock of the corporation, but his petition was not filed until more than five years after the original transaction, and the sole question discussed, and determined, by the Iowa Supreme Court, is with respect to

the statute of limitations. The court held that a demurrer to the petition of plaintiff was properly sustained, and affirmed the judgment of the court below.

As we pointed out in our original brief, the Iowa rule is that in determining whether there are actionable false and fraudulent representations, consideration must be given to the situation of the parties, the matters with which they are dealing, the subject matter in hand, the knowledge, and means of knowledge of the facts. Here respondent, a nation-wide investment house, was offering the Longview local improvement securities as desirable investments for the policy reserves of a life insurance company. Respondent was well known to petitioner as a large and reputable concern. Petitioner properly assumed that respondent had made some measure of investigation concerning the securities which it was offering, and relied upon its statements with respect thereto. Under such circumstances, no court, except the Seventh Circuit Court of Appeals in this case, has ever in effect held that the rule of *caveat emptor* may properly be applied to purchases of securities of the type and character here involved.

V.

The trial court properly ruled that the statements of the Wood letter of May 14, 1930, that

"We believe you have before you practically all the data," and

"You will observe that the city has no funded debt other than these improvement bonds,"

constituted representations that petitioner had been furnished all facts within respondent's knowledge, that there were no other similar securities outstanding, and that such representations were material. Whether such representa-

tions were false, and were relied upon by petitioner, were properly submitted to the jury by the trial court, and the determination of the Seventh Circuit Court of Appeals, that the letter was of "trivial materiality," substituted the judgment of the court for that of the jury on the weight of the evidence.

Under subdivision V of their brief, pages 65-71, counsel for respondent urge that since the Wood letter of May 14, 1930, was a written instrument, its construction as a representation involved a law question to be determined by the court. They further urge that the evidence shows that petitioner

"Did not rely on the statement (of the Wood letter) as a representation that there were no outstanding bonds of any other municipal body which were a charge upon lands within the improvement districts."

We agree, of course, that the proper construction of a written instrument presents a question of law for the court. We agree further that the materiality of a particular representation, whether written or oral, in fraud cases presents a question of law to be determined by the court, in the first instance. But, the question as to whether a particular representation was relied upon, and the extent of such reliance, presents an issue of fact for determination by the jury. Where the facts are in dispute, or conflicting inferences may be drawn from the testimony, no court has a right to substitute its judgment for that of the jury upon the weight to be accorded any item of evidence.

In the Wood letter, Exhibit "B-24," Hubbell was directly and specifically told:

"We believe you have before you practically all the data covering this issue of bonds, but if you have any questions in mind, we shall be pleased, indeed, to have you call Mr. Kelley or this office for anything you may

need. You observe, of course, that this city has no funded debt, other than these improvement bonds, and that the original debt has been materially reduced through retirement and maturity."

The language of this letter is plain and unambiguous. It could mean but one thing, namely,

"We have furnished you all the information in our possession concerning the bonds, but if you want more, we shall try to supply it."

The trial court properly ruled that this letter spoke for itself, and that it constituted a representation that respondent had already furnished petitioner "substantially all the data in its possession." The trial court also properly submitted to the jury the question whether petitioner relied upon such representation, and the extent of such reliance, as a fact issue.

Counsel complain that Hubbell did not testify as to his construction of the Wood letter, and his reliance upon its statements. The statement of the evidence in this case was prepared by counsel for respondent, and present counsel for petitioner did not see it before the preparation of the printed record in the Circuit Court of Appeals. The fact is, as counsel well know, that upon the trial, questions were propounded to Hubbell, calling for his construction of the Wood letter, and that the trial court sustained respondent's objections thereto. The trial court ruled that the Wood letter "spoke for itself," held that it did constitute a material representation, and submitted it to the jury.

The Circuit Court of Appeals holds that because of Hubbell's testimony that it was not his usual custom in 1930 to inquire into the extent of overlapping municipal issues, the Wood letter, while a careless statement for respondent to make, was of "trivial materiality." (R. 668) That court did not hold that the Wood letter should have been ex-

cluded from evidence, but said merely that the letter and its implications were of "trivial materiality." In other words, the Seventh Circuit Court of Appeals did not hold the letter inadmissible, and did not hold that the letter was not a representation that the Longview improvement bonds constituted the only outstanding securities of that type and character in Longview, but held that such representations were not relied upon, and were not entitled to be relied upon by petitioner. In this respect, it seems to us very plain that the Circuit Court of Appeals has merely substituted its judgment for that of the jury below upon a fact question.

At pages 66 and 67 of their brief, counsel urge that neither Wood, in writing the letter, nor Hubbell, in reading it, thought that the sentence in question, "had any reference to the Cowlitz County diking district bonds, or to the bonds of any other separate municipality." We are unable to see how such construction can be placed upon the plain language used by Wood in the letter. Here was a definite, positive statement that the city had no funded debt "other than these improvement bonds." Is the situation changed any by the conceded fact that Hubbell did not customarily make inquiry as to overlapping issues? Certainly not. Here was a definite, positive statement that the city had no funded debt "other than these bonds." Hubbell knew that these were not general obligation bonds; that they were no part of the funded debt of the City of Longview in the technical sense, but he accepted the Wood letter in the way in which it apparently was intended to be read, namely, that this issue was the only one outstanding at Longview.

Counsel for respondent cite the case of *Readinger v. Rorick*, 92 Fed. (2d) 140, in support of their contention that the Wood letter of May 14 does not constitute a misrepresentation as to the extent of the outstanding bonds. The bonds involved in that case were issued by an irrigation district, and the offering circular recited that the total

bonded indebtedness of the district was \$295,000. The statement was correct, but because of overlapping municipalities, that figure did not measure the total indebtedness against the properties embraced within the district. As we pointed out in our original brief, had Wood merely said in his letter of May 14 that the city had no funded debt, Hubbell would have clearly understood what he meant, for the city, it appears, had no general obligation bonds outstanding. But, when Wood went further, and stated that the city had no funded debt "other than these improvement bonds," the usual and ordinary meaning which would be applied thereto by persons familiar with the purchase of bonds, was, that, there were no other bond issues of similar character outstanding at Longview. In this respect, the representation was clearly false. The representation was a material one. A jury question was presented as to the extent of Hubbell's reliance thereon, and that question was properly submitted to the jury by the trial court under proper instructions. We submit that the Circuit Court of Appeals exceeded its powers, as a court, when it undertook to substitute its own judgment as to the sufficiency of the representation for that of the jury, which apparently resolved that question in favor of petitioner.

VI.

A mere reading of the opinion of the Seventh Circuit Court of Appeals demonstrates that it was predicated, in large measure, upon the thought that had petitioner adequately investigated the Longview improvement bonds, it would have discovered the true facts, and that its failure so to do bars recovery. This is directly contrary to the rule of law which prevails in Iowa.

On pages 71-73 of their brief, counsel for respondent urge that the Circuit Court of Appeals did not decide that

petitioner's negligence barred recovery for fraud. In our original brief we pointed out in considerable detail the repeated statements found in the opinion of the Seventh Circuit Court of Appeals, to the effect that had petitioner made an adequate investigation of the fact situation surrounding the bonds, it would have learned everything of which it now complains, and that "there is nothing to suggest why it could not have found them with equal facility before it purchased the bonds." (R. 671)

The quotations from the opinion set forth on pages 64 and 65 of our original brief, make it plain that the Seventh Circuit Court of Appeals was very largely influenced in arriving at the decision that it did by the belief that petitioner had not used adequate care to protect itself in the transaction. No amount of argument can change the plain language of the opinion below.

Counsel for respondent now admit that the issue of contributory negligence, under the Iowa law, was not in the case, and that petitioner's failure to conduct an adequate investigation, if established, constitutes no defense. Counsel's concession, however, cannot change the fact that the Circuit Court of Appeals for the Seventh Circuit did, in large measure, predicate its decision upon petitioner's failure to protect itself by adequate investigation. The brief of respondent on this division of the case merely emphasizes the error into which the Circuit Court of Appeals fell.

VII.

The Seventh Circuit Court of Appeals determined but one question, namely, that the evidence was insufficient to justify submission of the case to the jury, and that the trial court should have directed a verdict for defendant. No other assignments of error were considered or decided.

Under division VII, pages 73-83, inc., of their brief, counsel for respondent urge that the judgment of the Circuit Court of Appeals reversing the trial court should be sustained, even though this court concludes that the evidence is sufficient to justify submission of the case to the jury. Counsel urge that there was error in the instructions to the jury, that the trial court erred in admitting evidence, and that, in any event, there was no evidence before the jury from which it could determine the amount of petitioner's damages. It is to be observed that the Circuit Court of Appeals has never passed upon, or considered, these questions. Since the Seventh Circuit Court of Appeals did not specifically pass upon such questions, we doubt that this court will desire to consider or decide the questions thus raised. We have no objection, however, to meeting the questions, if the court feels that a determination thereof is proper at this time.

A.

The instructions of the court upon the question of damages state correct rules of law for the guidance of the jury.

The trial court in its instructions told the jury that if it found plaintiff (petitioner) entitled to recover damages, then

"The measure of plaintiff's damages is the difference, if any, between the actual value which the \$266,000 par value of Longview improvement district

bonds now held by petitioner had at the respective dates when the same were purchased by the petitioner from respondent, and the actual value which said bonds would have had on said dates if they had been as represented, if and to the extent that you find from the evidence said bonds were in fact misrepresented by the defendant (respondent).” (R. 404)

The measure of damages so given to the jury was in accord with respondent's requested instruction no. 9. (R. 399) The measure of damages for fraud in the sale of property, in Iowa, is the difference between the actual inherent value of such property, as it actually was at the time of sale, and its value had it been as represented. *Stokes v. Converse*, 153 Iowa 274, 133 N. W. 709, 711.

After stating the correct measure of damages, the court gave to the jury that portion concerning which complaint is made, appearing at R. pg. 404, and set forth in the footnote at the bottom of page 75 of respondent's brief. Counsel complain that the jury was not limited to a consideration of only those facts and circumstances “relating to the value of the bonds at the time they were acquired by petitioner as was disclosed by the evidence bearing on the issue of damages.” This is a purely hypercritical criticism of the instruction, for the jury were expressly told to take into consideration the facts and circumstances “as shown by the evidence, the local conditions then existing at Longview so far as shown by the evidence, the true financial condition of the Lumber Company and its subsidiaries, and all other facts and circumstances then existing, as shown by the evidence.”

The cases of *Garvey v. Chicago Railways Co.*, 339 Ill. 276, 171 N. E. 271; *Benham v. Heath*, 77 Ind. App. 91, 133 N. E. 179, and *Gallagher v. Singer Sewing Machine Co.*, 177 Ill. App. 198, do not support counsel's criticism of this instruction.

At pages 76-78, inc. of their brief, counsel vigorously attack the instruction of the court by which the jury were told that in determining the fair actual value of the local improvement bonds at the times the plaintiff acquired same, they might take into consideration subsequent events and developments.

No exception to the instructions upon the ground now urged was taken at the time of the trial. The only exception addressed to the instruction on damages was as follows:

"Mr. Johnston: I except to the modification of defendant's Instruction No. 9 by the addition thereto of the matter relating to the right of the jury to consider subsequent facts and circumstances in arriving at their determination of value as of 1930 when these bonds were sold, on the ground that such evidence should not be considered by the jury, and is not a proper element of damage." (R. 407)

It is elementary, of course, that a ground of exception to an instruction may not be urged upon appeal, which was not specifically called to the attention of the trial court. The claim now advanced by counsel, that by the instruction in question the jury was permitted to consider the effects of the depression, is not open to respondent, because no exception was taken upon that ground at the time of the trial.

Furthermore, the instruction which directed the jury to take into account subsequent developments, which were the result of conditions then existing, stated a correct rule of law. In *Whiting v. Price, et al.*, 51 N. E. 1084, the action was based on fraud in the sale of a corporate bond, which was represented as secured by a first mortgage upon real estate and franchises of a power company. The court instructed the jury that in determining the actual value of the bond, they might properly take into consideration "circumstances which have transpired, as shown by the evi-

dence." The evidence showed that the issuing company had been placed in receivership, and the bond had become practically worthless. The Massachusetts Supreme Court, in an opinion delivered by Mr. Justice Holmes, who later served with such distinction on this court, sustained the instruction, saying:

"We think that what was added to that express direction merely amounted to allowing the jury to take subsequent events into account in arriving at the two values at the time of the purchase, which the jury were directed to compare. We cannot say that this was wrong. The market value of the bond, at the time of the sale may have been illusory, because the public also may have been deceived. The statement which we have quoted, appearing in the bond of an electric light company, certainly conveys the impression that it has a plant and property, which naturally would include land. Or, if it be answered that the public, which makes market prices generally, looks a little further than such vague words, the question remains, what would have been the value of a bond adequately secured, when the public were willing to pay for one depending so far upon speculation for its value that subsequent events have shown it to be worthless? The subsequent events may be likened to the coming out of a latent disease existing in a horse at the time of a fraudulent sale, to take an example put by Cockburn, C. J., in *Twycross v. Grant*, 2 C. P. Div. 469, 544."

The federal courts have always followed a similar rule. In the case of *Hindman v. First National Bank*, 112 Fed. 931, the Sixth Circuit Court of Appeals, speaking by Judge Lurton, later an associate justice of this court, said:

"Where the subject of the purchase is tangible property, the real actual value and the market value are for the most part one and the same. But market sales of corporation shares may not be any real indication of real intrinsic value."

The true inquiry will be, what was the real, intrinsic value of the shares bought by plaintiff, for his dam-

ages must be reduced by deducting that value. What-
ever tended to show the want of intrinsic value of shares
in a company in the circumstances of this company at
the time of the purchase was competent evidence."

Iowa follows the same rule. Thus, in *Baumchen v. Donahoe*, 215 Iowa 512, 242 N. W. 533, plaintiff was induced to subscribe to stock of a reorganized bank, by representations that all questionable paper in the original bank had been eliminated. About two years after plaintiff purchased his stock, the reorganized bank went into receivership, and was liquidated. The difficulties were largely due to unsatisfactory paper which proved worthless, and which had not been eliminated in the first reorganization. Plaintiff was required to pay an assessment equalling the par value of his shares. The trial court submitted the case to the jury, instructing that plaintiff might recover the amount of his original purchase price, plus the amount of the assessment which plaintiff was compelled to pay, if the plaintiff established "by a preponderance of the evidence that the assessment was directly caused by the condition of the bank at the time he purchased said stock, and was not caused by anything that took place in the intervening time." The Iowa Supreme Court affirmed the judgment of the trial court, which awarded plaintiff not only the amount paid for his stock, but the amount of the additional assessment thereon.

In view of these authorities, we submit that the attack made on the instructions of the trial court, merely because thereby the jury were permitted to take into consideration subsequent events, must fail.

VII.

B.

Evidence of events subsequent to 1930, in connection with the Longview local improvement bonds, was competent, and was properly admitted by the trial court, and the effect to be given such evidence was properly covered in the court's instructions to the jury.

At pages 79-81, inc., of their brief, counsel urge that the trial court received incompetent evidence. The evidence as to which complaint is made is summarized under six divisions set forth at pages 80 and 81 of their brief. This evidence was all material and competent, and properly received by the trial court. It is almost universally held in actions of this character, that the amount received by a plaintiff on a foreclosure action may be shown in evidence. See the leading case of *Hotaling v. A. B. Leach & Co.*, 247 N. Y. 84, 159 N. E. 870. So, it was competent for petitioner to show that The Long-Bell Lumber Company was relieved of its guarantee of the local improvement bonds by proceedings under Section 77-B of the Bankruptcy Act, and that by virtue of the plan of reorganization approved by the court in that proceeding, petitioner received in lieu of such guarantee, for each \$1,000 bond, slightly more than eight shares of common stock in the reorganized corporation. The value of this stock is likewise shown and tendered as a credit upon petitioner's claim.

The next general class of evidence which it is claimed was improperly received by the trial court related to certain proceedings had in Cowlitz County, Washington in the years 1937 and 1938, by which the lien of unpaid general taxes was foreclosed as to the lands embraced in the local improvement districts, and thereby the lien of the local improvement district assessments was completely wiped

out. The court will recall that The Long-Bell Lumber Company and its subsidiaries paid the local improvement assessments falling due in the year 1930, but defaulted upon those falling due in 1931 and subsequent years. The Lumber Company failed to pay its general taxes due in 1932, and this default led to tax foreclosure proceedings, which resulted in a tax deed covering more than sixty per cent in area of the Longview property. This evidence was competent for several purposes. It was competent to show that the lands were so heavily burdened with diking and local improvement district assessments that the owners of the property, shortly after the bonds were purchased by petitioner, elected not to pay even the general taxes thereon. In *Hindman v. First National Bank*, 112 Fed. 931, the Circuit Court of Appeals for the Sixth Circuit pointed out that the only way by which the actual, inherent value of securities purchased at a particular time may be shown, is by a consideration of subsequent events, and developments, which are the direct result of conditions then existing. All evidence of subsequent events received by the trial court tended to show the want of intrinsic value in the securities at the time of the sale, and was competent for that purpose.

The last item of evidence which it is claimed the trial court improperly received, was a supplement to the 70th Annual Report of petitioner to its policyholders, containing a list of the bond investments held by petitioner on December 31, 1936, and the values at which the bonds were carried upon the books of petitioner on said date. This evidence was not offered, as counsel would have the court believe, by petitioner, for the purpose of showing values, but merely to meet certain evidence which was brought out first in cross examination of F. W. Hubbell, petitioner's vice president and treasurer. While Mr. Hubbell was on the stand under cross examination, counsel for respondent de-

veloped that he had verified both the original and amended complaint in the action, in which certain statements were made as to the intrinsic value of the Longview local improvement securities. Following these inquiries, in an effort to impeach Hubbell, and to place him in a questionable light before the jury, counsel for respondent presented to Hubbell defendant's Exhibit "8," which was a supplement to the 69th Annual Report of petitioner to its policyholders, as of December 31, 1935. This report disclosed that petitioner owned on that date \$272,000 par value of Longview improvement bonds, carried on its books at a valuation of \$231,200. (R. 202)

In order to meet the effect of the cross examination of Hubbell, counsel for petitioner, upon redirect examination, questioned him concerning the methods followed by petitioner in determining the book value of securities. Hubbell testified that the book values of securities were regulated by instructions of the various insurance departments, and that barring clerical errors, petitioner undertook to comply with such instructions. Plaintiff's Exhibit "B-50" and Exhibit "B-51" were then offered in evidence, which disclosed that the National Association of Insurance Commissioners' Convention treated the Longview improvement bonds in 1935 as current, and permitted them to be carried on the books at an amortized value. As of December 31, 1936, the Insurance Commissioners' Convention prescribed a valuation of "ten flat," meaning ten per cent of the par value, without accrued interest. The 70th Annual Report of petitioner to its policyholders, and the 72nd Annual Report disclosed that petitioner was carrying the \$266,000 of Longview bonds on December 31, 1936, at a valuation of \$26,600, and on December 31, 1938 at \$18,620.

These exhibits were offered and received only for the purpose of meeting the inferences left in the minds of the jury by the cross examination of Hubbell, and the use of

the 1935 report to policyholders, defendant's Exhibit "8".

By his cross examination, counsel for respondent sought to create the impression in the minds of the jurors that in December, 1935, petitioner regarded the bonds as worth substantially more than it had alleged in its original complaint, or that it was deliberately misrepresenting the value of its assets to its policyholders. Counsel for respondent first brought into the case, upon his cross examination of Hubbell, the element of book value of the Longview improvement bonds. Upon redirect examination it was perfectly competent and proper for petitioner to show the manner in which the statement, Exhibit "8" was prepared, and the manner in which the valuations there shown were arrived at. It was likewise proper for petitioner to correct the impression created by the cross examination, that petitioner was misrepresenting the value of its assets in its reports to its policyholders. There is nothing in the admission of these exhibits of which respondent may justly complain. The whole matter was clearly within the discretion of the trial court. Respondent may not now complain of the admission of these exhibits, which were offered merely for the purpose of explaining and clarifying a situation which was first inquired into on cross examination of petitioner's vice president and treasurer.

VII.

C.

There was evidence before the jury justifying the verdict of Sixty-six Thousand One Hundred Fifty Dollars (\$66,150).

At pages 81-83, inc., of their brief, counsel urge that there was no evidence before the jury enabling it to determine the amount of petitioner's damage, and that even

though all other contentions fail, the judgment of the Circuit Court of Appeals reversing the trial court should be sustained on this ground alone. This contention, upon examination, proves to be without support in the record.

The local improvement bonds were never listed upon any exchange. The market for such securities was made and controlled by respondent. That this was true, particularly of the local improvement bonds, is amply demonstrated by the record. Harold L. Stuart, respondent's president, on February 28, 1929, wrote the president of the Lumber Company, in which he made claim for \$75,000 for services, in bringing about an improvement in the market position of Long-Bell's securities. In this letter, referring to the retirement of Long-Bell mortgage bonds under the sinking fund provisions of the mortgage, Stuart said:

"We shall be very pleased to act for you in getting these bonds in and there is no question but what we can do better for you than anybody else, because we know where the bonds are. I also took the liberty of suggesting to you that, if you ask us to do this, you should not ask anybody else to work on these bonds, as the result could only be expensive to the Company. In the last analysis we are the market on Long-Bell securities, except possibly very small amounts, and you can understand how quickly we feel a movement in Long-Bell bonds when the fact that you had spoken to a Kansas City dealer about them was immediately reflected in our office here." (R. 432)

During the earlier months of 1930, respondent was shown to have purchased a number of the Longview improvement bonds at prices ranging from 95 to 98. In October, 1930, respondent purchased a \$200,000 block of the bonds from B. M. Baruch of New York, at a price of 89. (R. 285-287) These facts amply demonstrate that there was no real market on the Longview improvement bonds, except that made by respondent in purchasing and resel-

ling the securities. Respondent completely controlled this market, and, in fact, fixed the prices.

There was a large volume of evidence before the jury bearing on the question of damages, and that body was able to, and did, determine the value of the Longview bonds, had they been as represented; and also their actual, inherent value at the various times they were purchased by petitioner. There was ample evidence from which the jury could properly have concluded that had the bonds been as represented, they would have been worth approximately par. The price paid for a security, under particular representations, may be considered by the jury in determining its value, had it been as represented. The first \$100,000 of Longview improvement bonds acquired by petitioner were exchanged for a like amount of Louisiana State Highway Bonds maturing in the early part of 1931. The Louisiana bonds were shown to have been 5% coupon bonds, and were worth slightly in excess of par on the market in May, 1930. The other large transaction consummated between the parties involved an exchange of \$200,000 Chicago Tax Anticipation Warrants for a like amount of Longview improvement bonds on October 16, 1930. The Chicago Tax Anticipation Warrants then had a value of slightly above par. They bore 6% interest, and were payable out of the 1929 tax revenues of the City of Chicago, as collected. (R. 273)

The evidence shows that the highest grade municipal securities in May, 1930, and in October of the same year, were selling in the market at prices to yield the purchaser an interest return of $4\frac{1}{2}\%$, or slightly above. (R. 186) The Longview improvement bonds were not general obligation bonds payable from general tax revenues, but solely from the proceeds of special assessments levied against benefited real estate, and from the guarantee of The Long-Bell Lumber Company. In view of the record, we submit that

the evidence was amply sufficient to justify a jury in concluding that had the bonds been as represented, their market value would have been approximately par. The bonds purchased by petitioner for cash were bought at 99 3/4.

The jury likewise had before it a large volume of testimony from which it could properly determine the actual, inherent value of the Longview improvement bonds on the dates they were purchased. Counsel for respondent, in their brief, apparently take the position that petitioner was under the obligation of introducing so-called "expert testimony" to show the actual, inherent value of the bonds, rather than to show, as petitioner did, the circumstances surrounding the bonds, and the factors entering into the true value thereof, and permit the jury to fix the value. We are aware of no rule of law that requires "expert" testimony as a necessary prerequisite to the recovery of damages by a defrauded purchaser.

There were two elements which gave the Longview improvement bonds value in the summer and fall months of 1930. The first of these was the assessments upon the Longview real estate, from which the bonds, by their terms, were payable, and second, the unconditional guarantee of The Long-Bell Lumber Company. The jury had before it a large amount of evidence bearing upon the value of both factors. The evidence disclosed in great detail the local conditions existing at Longview in the summer and fall of 1930. The topography of the land, the character of the soil, the location of dikes and ditches, the location of industries and business establishments, the manner in which the city had been laid out, the extent of the improvements constructed, and the prospects for future expansion, were all shown in considerable detail in the testimony of Horace A. Dryer. (R. 274-284). The amounts of the Longview improvement bonds outstanding in each of the districts were shown. The amounts of the assessments upon typical lots

in each of the various districts were disclosed, as well as the amounts of the assessments upon the same lots for the diking district.

The evidence disclosed that the Lumber Company had engaged in an intensive sales campaign to dispose of its Longview real estate for a number of years prior to 1930. Notwithstanding the activities of this real estate organization, by April, 1928, the sales of lots had so declined, that, in that month, new sales were slightly less than \$15,000, while forfeitures of existing contracts amounted to \$17,000. The evidence discloses that real estate activity at Longview declined as the depression in the lumber business became more evident in 1928, 1929 and 1930. It was very clearly established that by May or June, 1930, except for a few desirable lots, practically all of the vacant, unimproved real estate in Longview could not be sold at prices equal to the combined diking and local improvement district assessments.

Under these conditions, it is obvious, just as Mr. Dryer testified, that in May and June, 1930, there was little or no prospect that the vacant, unimproved areas of Longview real estate could be marketed at any figure. About one-third the area of Longview was platted into lots and blocks, and two-thirds was mere unplatted acreage. There were some 5,000 platted lots embraced within Longview. On December 31, 1927, 2,629 of these lots had been sold, 2,062 were unsold, and 419 were reserved from sale. The lots sold included those sold to R. A. Long, personally, so that the number sold to individual investors was somewhat less than half of the number of lots then platted, or less than one-sixth of the total unimproved area within the Longview city limits.

The jury had before it aerial photographs of Longview, taken, in the year 1930, about the times petitioner's bonds were purchased. These photographs covered practically

every part of the city, and graphically illustrated the local conditions, the great distances separating the various portions of the city, and the intermediate vacant tracts of wholly unimproved land.

The jury had before it the fact that there were large areas of wholly unimproved property, which had been subjected to very burdensome assessments in Districts Nos. 11 and 19, as well as in the diking district. Exhibit "P-49", one of the exhibits certified to this court, discloses that the assessments, upon various unimproved tracts in the diking district alone, varied from \$200 to \$2,500 per acre. The Long-Bell Lumber Company, as the owner of the great bulk of the real estate within the City of Longview, and guarantor of the bonds, was in practical effect, the only source from which the bonds could be paid.

In addition to all this evidence with respect to the local conditions at Longview, the jury had before it a considerable volume of testimony bearing upon the value of the Long-Bell guarantee in the months of May to October, 1930. When the Longview improvement bonds were first presented to petitioner, The Long-Bell Lumber Company was actively considering the formation of the Sales Corporation, to which all of its liquid, unencumbered assets were subsequently transferred. The jury had before it the fact that Long-Bell was suffering operating losses at the rate of approximately \$100,000 per month during the first six months of 1930. The Longview local improvement bonds, by their terms, did not mature until 1937, 1938 and 1939. From the evidence, the jury was justified in concluding that the Long-Bell guarantee of payment at the maturity of the bonds some seven to nine years distant, while giving some additional value to the bonds, fell short of indicating the probability of ultimate payment.

The jury had before it the evidence that because of Long-Bell's top-heavy structure of bonded and guaranteed

debt, it was forced into bankruptcy under the provisions of Section 77-B of the Bankruptcy Act in 1934. Under this proceeding the Long-Bell guarantee was wiped out, and in lieu thereof, for each \$1,000 bond, the local improvement bondholders received only eight shares of common stock in the reorganized corporation. When the reorganization plan became effective in December, 1935, the value of this stock was approximately \$10 per share. As petitioner owned \$266,000 par value of these bonds, it was entitled to receive approximately 2,300 shares of new Long-Bell stock, having a value at that time of approximately \$23,000. The jury, of course, had a right to find that the amount received in the reorganization proceedings in 1935 was not conclusive as to the actual value of the Long-Bell guarantee in May and October, 1930.

The jury had before it the fact that practically every local improvement district assessment upon unimproved property in Longview had been wiped out by the foreclosure for general taxes, which had culminated in the tax deed. The jury had before it the amounts remaining in the hands of the City Treasurer of Longview in each of the local improvement district funds, which showed that there was no prospect that any further bonds could, or would, be retired through payments of additional assessments.

The Long-Bell guarantee had been supplanted by common stock in the reorganized Long-Bell Corporation, which had a value of approximately \$23,000. Petitioner's loss, as the result of its investment in Longview improvement bonds, therefore, was at least \$240,000. The verdict of the jury was for \$66,150. It is obvious that the jury was not actuated by any feeling of passion or prejudice, for it might well have returned a much larger verdict. It was for the jury to determine the amount of petitioner's damage. Respondent was indeed fortunate that the verdict was not for a substantially greater amount.

In recent years the courts have almost universally recognized that in cases of this kind, particularly where the market is made or controlled by the investment house issuing the bonds, the prices at which bonds sell, shortly after their issue, have little or no relation to the actual, inherent value of such securities. The rule is now well established, in the majority of jurisdictions, that where the facts concerning an issue of bonds, which have been misrepresented, are placed before the jury, that body may properly determine from subsequent events, the actual, inherent value of the securities at the time of their sale, and that under such circumstances, the evidence is sufficient to sustain a verdict for plaintiff.

Perhaps the leading case in this country on this question is that of *Hotaling v. A. B. Leach & Co.*, 247 N. Y. 84, 159 N. E. 870. In that case it appeared that plaintiff had purchased from the defendant, an investment house, a 7% bond of the National Oil Company, at a price slightly below par. The oil company was a holding concern, which owned refineries, transportation and marketing facilities. A depression occurred in the petroleum business shortly after the bonds were issued, and in about one year after the bonds were sold, the company went into receivership; its properties were sold at foreclosure sale, and a purely nominal sum was realized therefrom by the bondholders. The case was tried to the court without a jury, which rendered judgment for the amount paid for the bonds, less the amount realized from the foreclosure sale. Leach & Co. appealed. It conceded the sufficiency of the evidence on the issue of fraud, but attacked the judgment solely on the ground that the evidence was insufficient to justify any award of damages. The New York Court of Appeals and Errors, in an exhaustive opinion by Judge Lehman, held the evidence sufficient to sustain the award of the trial court, and affirmed the judgment. In the course of the opinion, the court said:

"In the present case the question is complicated by two circumstances. The property purchased is a bond, a chose in action whose intrinsic value is dependent solely upon the debtor's ability to pay when payment becomes due, and in addition the bond was recommended as an investment and defendant was informed that it was bought for that purpose. Even if we had evidence upon which a definite estimate might be made of the value of the company's property which was covered by the trust indenture and constituted security for the bond issue, we should not be able to fix with certainty the value of the bond. The oil company held the stock of subsidiary companies which in turn owned the tangible assets. The stock of the subsidiary companies was pledged, their tangible assets were still at the risk of the business. Probability of payment of the bond issue depended primarily upon the success of the business and its efficient management. Though the company might not have failed if conditions in the oil trade had not become disturbed, there is room for inference upon this record that these disturbed conditions would not have caused the failure if the enthusiastic statements of the value of the company's assets contained in the circular had been true. On the other hand, if a complete and accurate picture had been given of the oil company's position, an expectant investor might have hesitated and drawn back with a reasonable fear that any adverse change in business conditions would bring ruin to the company. That ruin came with change of conditions. The effect of the representations of the defendant did not cease with plaintiff's purchase. He continued to hold the bond for investment in accordance with the defendant's recommendation. Loss of his investment followed because the weakness of the company had been concealed from him by defendant.

* * * The loss proximately caused by the defendant's fraud is the difference between the price he paid and the value of what he received when put to the use contemplated by the parties. In this case that value must be determined in the light of subsequent events. As long as the fraud continued to operate and to induce the continued holding of the bond, all loss flowing

naturally from that fraud may be regarded as its proximate result. Change of conditions may have been a subsidiary cause; it was not an independent cause. The loss sustained is directly traceable to the original misrepresentation of the character of the investment the plaintiff was induced to make."

The court concluded its opinion with these words:

"For these reasons, we find in the evidence, sufficient basis for the rule of damages applied."

A similar case from the New York courts is that of *Crandall v. A. B. Leach & Co.*, 223 N. Y. Supp. 127. The bonds purchased by plaintiff in that case were of the same issue as involved in the *Hotaling* case, and the same fraud was charged. Plaintiff introduced evidence showing that the trust indenture securing his bonds had been foreclosed, and that he had received but \$5.84 for each \$1,000 bond. The trial court excluded this evidence, but submitted the case to the jury, which returned a verdict in favor of plaintiff. The trial court then set the verdict aside, and rendered judgment dismissing the plaintiff's petition; on the sole ground that the evidence of damages was insufficient to support any recovery. The Appellate Division of the New York Supreme Court reversed the trial court; and in the course of the opinion said:

"Studying the picture as a whole, no great difficulty should be encountered in an arrival at an approximate value of the bonds in question from January to March, 1920, and, as we view it, there was sufficient evidence from which a jury might have in its judgment determined that at the time of the purchase they were intrinsically worth much less than the sum plaintiff paid for them. The National Oil Company was a holding company. Its properties were owned by other corporations subsidiary to it, and its control thereof rested upon its ownership of the stock of those subsidiaries. This was the only pledge to secure the bonds in ques-

tion, so that the actual properties but indirectly supported their value. . . .

A number of other exceptions are called to our attention, but in view of this conclusion ~~only~~ one of them need now be mentioned. A new trial must be had, and it therefore seems best to point out that the foreclosure decree under which the property was sold, while not a final determination of the value of the bonds, either at the time of their purchase by plaintiff or later, was nevertheless competent evidence for the jury to consider on the question of their value, as well as for the purpose for which it was admitted, and that its exclusion from consideration on the question of damages was error."

Most of the courts, both state and federal, which have had occasion to pass upon the question presented in the *Hotaling* and *Crandall* cases, have arrived at similar conclusions. Such was the decision of the Iowa Supreme Court in *Baumchen v. Donahoe*, 215 Iowa 512, 242 N. W. 533. The Sixth Circuit Court of Appeals arrived at the same result in *Hindman v. First National Bank*, 112 Fed. 931, and see *Paul v. Cameron*, from the Supreme Court of Nebraska, 256 N. W. 11.

Some jurisdictions have adopted the rule that the measure of damage will be limited by the actual, inherent value of the securities at the time of the discovery of the fraud. Iowa, however, has not seen fit to follow that rule. The proof adduced in the instant case was sufficient to support the verdict of the jury for \$66,150. The fixing of the damage was the exclusive province of the jury. The record presents nothing in this respect of which respondent can properly complain, and the Circuit Court of Appeals did not base its reversal of the judgment upon any lack of proof as to the amount of petitioner's damage.

CONCLUSION.

That respondent made false representations concerning the location of the Long-Bell, Weyerhaeuser, Longview Fibre, and other industrial properties, and the frontage of the city upon the Columbia River, is conceded by every one. We have pointed out that the evidence was amply sufficient to justify the jury in finding that respondent's officers, on numerous and oft-repeated trips to Longview, could not well have failed to discover the true facts with reference to the location of the corporate limits of the city.

✓ The record clearly justified the jury in the trial court, in finding that respondent indulged in half-truths, made false and misleading representations with respect to the financial condition of The Long-Bell Lumber Company, both by affirmative misrepresentations, and by suppressing the true facts within its knowledge. The representation of the Wood letter of May 14, 1930, that petitioner had been furnished "substantially all the data," was a material representation, and the Circuit Court of Appeals merely substituted its judgment for that of the jury in holding that the recitals of that letter were of "trivial materiality."

The Circuit Court of Appeals for the Seventh Circuit erroneously determined that the so-called "hedge clause" of the offering circular afforded to respondent a defense to the charges of fraud. Counsel for respondent, in their brief in this court, concede that the hedge clause constitutes no defense to misrepresentations of fact, whether deliberately made, with knowledge of their falsity, or recklessly made, with no reason to believe that the statements were true. The Seventh Circuit Court of Appeals, as we have pointed out, erroneously held that the hedge clause constituted a defense.

The decision of the Circuit Court of Appeals for the Seventh Circuit goes far beyond any other reported case,

is without support in judicial precedent, and is based upon clearly untenable grounds. Well established principles of law, applicable to this case, require that the judgment of the Circuit Court of Appeals be reversed, and that the case be remanded to that tribunal for further proceedings.

Respectfully submitted,

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